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Strategic motivations for Sino-Western alliances: a comparative analysis of Chinese and Western alliance formation drivers

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Abstract

This paper compares the key drivers of Sino-foreign alliance formation from the perspective of both Chinese and Western alliance partners. Our results indicate that Chinese companies enter into alliances with Western companies mainly to get accesses to international markets and to develop their technological and managerial competences further, while Western partners aim to gain access to the local customer and supplier bases of their Chinese counterpart as well as to the complex distribution systems found in the Chinese market. In analyzing the differences among Chinese and Western alliance motives, this paper shows how the initial deficiencies in the Chinese institutional environment has shaped the strategic motives of local companies and consequently lead to the diverging alliance formation motives in Sino-foreign alliances.

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Introduction

Quite aware of the potential benefits of securing a competitive position in the 1.3 billion-consumer market of China, an increasing number of Western multinationals are establishing alliances with local Chinese firms. Chinese alliance partners can offer instant access to established customer and supplier bases as well as to the complex Chinese distribution system. Western partners can further benefit from the local firm's contacts, experience and credibility hence gathering valuable opportunities for strategic learning (Jaegersma, 2005). However, given that alliances with local Chinese firms have become an important value-creating strategy for many Western multinational companies, it is striking how poor the performances of many alliances remain. One major cited reason for alliance failure is the incompatibility of alliance partners, where missing to establish and communicate compatible objectives can lead to insuperable problems for the process and outcome of the alliance (Dacin, Hitt and Levitas, 1997)

Particularly, divergences in alliance motives can lead to conflict situations, where alliance partners hold different expectations about the goals of the alliance. Especially in cross-border settings, alliance partners are likely to differ in terms of strategic intentions and alliance objectives (Slocum and Lei 1993; Dacin, Hitt, and Levitas, 1997; Demirbag, Mirza, and Weir, 1995; Tallman and Shenkar, 1990; Yan and Gray, 1994). Therefore it is imperative to investigate the strategic motives of potential alliance partners in order to avoid premature and unfruitful termination of the alliance. In this regard, the common underlying strategic motives of Western companies to enter into alliances with Chinese companies have been well researched (Beamish, 1993; Glaister and Wang, 1993; Teagarden and Glinow, 1991; Child et al., 1990). However, with a few notable exceptions (Dong and Glaister 2006; Hitt, Ahlstrom, Dacin, Levitas and Svobodina, 2004; Luo, 1997, 2002) little is known about the underlying motives of Chinese companies to enter alliances with Western partners. Surprisingly, despite the enormous increase in the number of Sino-Western alliances, the subject of strategic motives of Chinese alliance partners has received scant attention in the academic and management literature. To fill this void in extant international alliance literature, this chapter investigates the key drivers of international alliance formation from the perspective of Chinese companies. Particularly, this chapter aims to answer the questions how and why strategic motives of Chinese alliance partners differ from their Western counterparts.

By answering these questions this chapter addresses a main deficiency in international alliance literature that has so far given little attention to the perspective of local companies domiciled in rapidly developing countries (Hitt, Ahlstrom, Dacin, Levitas and Svobodina 2004; Luo 2002; Yan and Gray 1994). We intentionally depart from previous research in this field by providing a comprehensive analysis of the strategic motives of local companies based upon an extensive literature review of original Chinese research. We choose to focus on primarily Chinese academic literature because it is reasonable to assume that Chinese companies are less reluctant to provide information on their alliance motives to Chinese scholars than to foreign researchers. Furthermore, Chinese scholars are often closely networked with Chinese companies and have a profound knowledge of the culture and ways of doing business in Chinese companies. Hence, we find that Chinese studies are better able to provide us with unique insights into the Chinese view on strategic alliance motives. We are therefore able to provide a comprehensive analysis of the Chinese perspective on international alliance motives to the Western audience. In order to validate our findings we have also conducted interviews with eight leading Chinese alliance companies in order to fully grasp the underlying motivations of international alliance formation. The remaining of the chapter will firstly review the merits and challenges of establishing alliances in general, highlighting the importance of partner motives compatibility in cross-national settings. Secondly, we provide an overview of the main motives of Western multinationals to enter China via alliances. The third section presents our results on the main strategic motives of Chinese alliances to enter into alliances with Western firms. This is followed by an extensive discussion on why underlying strategic motives of Chinese and Western alliance partners differs. We conclude with the main findings and managerial implications for both Chinese and Western alliance partners.

Strategic motivations and compatibility of alliance partners

Strategic alliances are increasingly vital to a company's competitive survival (Das & Teng 2000; Doz & Hamel, 1998; Gomes-Casseres, 1996; Yoshino & Rangan, 1995, Combs & Ketchen, 1999; Ireland, Hitt & Vaidyanath, 2002). The surge in alliance activity can be observed particularly in knowledge-based industries, where the increasing costs of R&D in combination with a shortening of product and technology lifecycles have made it almost impossible for companies to develop technologies on a stand-alone basis (Teece, 1987; Hamel et al., 1989; Borys and Jemison, 1989; Erramilli and Rao, 1990; Hamel, 1991, Eisenhard and Schoonhoven, 1996; Combs and Ketchen 1999; Das and Teng 2000). As a single company has rarely the full range of knowledge or expertise, firms increasingly use strategic alliances to perform activities together that neither could perform alone. However, the potential synergy effects of alliances can rarely be actualized; failure rates up to 70 percent come as no surprise to many practitioners (Bleeke and Ernst, 1993; Park and Ungson, 2001). As Dacin, Hitt and Levitas (1997) emphasise, the incompatibility of alliance partners is found to be among the most important reasons for alliance failure. Diverging alliance motives among partners lead to conflict situations, hindering the successful implementation of the alliance. Especially in cross-border settings, alliance partners are likely to differ in terms of strategic intentions and alliance objectives (Slocum and Lei 1993; Dacin, Hitt, and Levitas, 1997; Demirbag, Mirza, and Weir, 1995; Tallman and Shenkar, 1990; Yan and Gray, 1994). Particularly, considerable heterogeneity in institutional environments (Peng & Heath, 1996), and asymmetry in resources and capabilities (Hitt, Dacin, Levitas, & Borza, 2000) are expected to affect the strategic alliance motives of firms.This is especially important where differences in culture, infrastructure, economic development and government policies increase the complexity of the context in which the alliance is embedded (Slocum & Lei 1993). In particular, the cultural heritage of a nation has been suggested to strongly influence the strategic orientations of company executives, resulting in different managerial ideologies that eventually affect the strategic decisions processes within the organization (Hitt, Dacin, Tyler & Park, 1997). Further, differences in levels of economics development are found to impact alliance motives of respective companies, where firms from developed economies predominantly seek local partners for market access, political connections and to fulfil local government's requirements for foreign investments. Conversely, firms from developing economies are found to seek access to technology, export opportunities and to gain international alliance experience. Following this logic, Beamish (1988) concludes that partners may differ significantly by economic development levels with respect to alliance motives and expected benefits. Further, as Hitt et al (1997:7) point out, "differences in government support and foreign investment policies can influence the alliance process. Government support in the form of national and industrial policies can motivate certain forms of industrial development."

While it is unlikely that alliance partners may have complete agreement on alliance objectives and expected benefits, a careful selection of alliance partners can increase the likelihood of at least complementary alliance motives. As Dacin, Hitt and Levitas (1997:4) stress "the need to understand both partner's similarities and differences in alliance objectives and strategic intentions is paramount in ensuring the success of alliances."

In the following we briefly present the main motivations of Western companies to enter into Chinese alliances.

Major drivers of Sino-Western alliances: the Western perspective

Extant literature on Sino-Western alliances has examined the strategic motives of Western alliance companies in China extensively; indicating that the main motives of Western companies to enter alliances with Chinese partners include faster entry into the Chinese market (Beamish, 1993), facilitation of international expansion (Glaister and Wang, 1993), conformation to host government policy (Teagarden and Glinow, 1991), as well a low cost sourcing (Child et al., 1990). Particularly, access to the Chinese market is considered to be the most importance alliance drivers for Western companies. As the Chinese market is expanding, and increasing share of consumer is gaining purchasing power. To tap into this market, Western companies were long required to establish joint ventures with local Chinese firms. However, since the China entered the WTO in 2001, foreign companies are no longer required to partner with local firms in order to invest in most high –tech industries. Nevertheless, Western companies still opt for alliances, as to get key access to rising industries as well as to established customer, supplier and distribution networks in the country (Jagersma 2002). The merits of allying with local firms lies in the ability of the Chinese partners to provide country-specific knowledge, contacts with regulatory authorities, and management of the local workforce (Inkpen and Beamish, 1997). In particular, alliances where technology constitutes an important component, Western firms are able to leverage resources and capabilities from local partners and adapt products to the local Chinese market (Wu and Callahan 2005).

Especially, in comparison to setting up wholly owned foreign subsidiaries in China, allying with local firms offers the superior advantage of maintaining flexibility in an unfamiliar and turbulent business environment. Chinese alliance companies often have complementary skills, resources and more easy access to Chinese markets and distribution systems, reducing the initial required start up investment by Western companies. Further, as the government retains great influence in the Chinese market, allying with local partners that have strong government relationships enables the Western company to overcome barriers in the local markets; particularly in IT sectors where the Chinese government plays a dominant role in determining technical standards (Wu and Callahan 2005). Hence, a key motive of Western companies to form alliances with Chinese firms is to build favourable relationships with (state-owned) organisations that have influence on these technical standards. In comparison to wholly owned subsidiaries, alliances with local Chinese firms facilitate the access to external complementary skills and resources while retaining flexibility for the Western counterpart.

Methodology and data

To provide a comprehensive analysis on Chinese alliance motives this chapter draws on both primary and secondary Chinese sources. A thorough literature review on Chinese written alliances studies has been carried out, complemented by structured interview with eight Chinese alliance companies. All eight companies were selected on the presence of international alliance experience. To ensure a balanced mix, we interviewed local companies of different size and industries. The experts, native planning or general managers were selecting on basis of their established reputation in the field of alliances and ability to sufficiently contribute to the goal of the interviews. To facilitate the interviews, a questionnaire was designed in Chinese and presented to the interviewees. The interviews lasted between thirty to sixty minutes and contained questions about company demographics (size, location and sales volumes) and -strategic motives to enter international alliances. Strategic alliances were defined to include strategic supplier relationships, minority stakes, joint ventures, cross-licensing arrangements, joint marketing agreements and research consortia. We excluded mergers, acquisitions, internal alliances, franchising, simple licensing, and non-strategic supplier relationships from our definition. Specifically, our questions did not target individual alliances, but respondents had to consider the entire alliance portfolio when answering the questions. Shifting the level of analysis from individual alliances to the alliance portfolio of companies is more likely to generate a comprehensive overview of the company's alliance activities and experience. As the average alliance portfolio of firms in our dataset consisted of 13 alliances, the total dataset refers to 104 alliances. Figure 2 indicates that only 25 % of the companies in our sample had formed more than 20 alliances over the last five years. While the percentage of international alliances constitutes a relatively small share of the entire alliance portfolio of the companies in our sample, the total dataset nevertheless refers to 32 international alliances. In line with earlier studies (Kale et al., 2002; Duysters and Heimeriks 2007), the number of alliances that a firm has formed can be used as a proxy for alliance experience. With an average of four international alliances, we can reasonable assume that the responding companies have some basic experience with international alliance partners. The responding companies were selecting from a variety of industries: 50% of companies in our sample operate in the automobile industry, while the remaining companies are in the pharmaceutical, software, telecommunication and construction industries. The majority of companies (75%) in our sample are large, with an employee base greater than one thousand persons. Only 25% are small sized companies with a maximum employee base of 500 people. 50% of companies that we interviewed are located in the Wuhan province; the remaining ones are based in Liuzhou (Guangxi province) and Neimenggu.

Regarding the Chinese alliance literature, we present here the main findings of an extensive review. Noteworthy, all sources reviewed agreed on the major motives of international alliance formation for Chinese firms. In the following we present a summary of our findings on major alliance motives of Chinese firms.

Major drivers of Sino-Western alliances: the Chinese perspective

Chinese studies report that the key objective of Chinese companies entering international alliances is to gain access to international markets (Zhang, 2007; Yang 2006; Liu 2005; Gu 2003; Ti Kan Mu, 2003). In particular, Chinese studies report that especially after the entry of China to WTO in 2003, local Chinese firms have increasingly pursued alliance with international partners (Ti Kan Mu, 2003; Liu 2005). Chinese companies report that allying with Western partners allow them to rely on the partner's established distribution and marketing channels in order to enter foreign markets (Liu 2005, Chen and Wang 2002). Similarly, Chinese partners aspire to learn about the dynamics and requirements of foreign markets by help of their Western partners (Wu 2007). Another important strategic motive for Chinese companies is to gain access to advanced technologies of the Western partner firm (Ti Kan Mu 2003; Wang 2007; Liu 2005; Lin and Guo 2005; Chen and

Wang 2002; Wu 2007; Liang 2005; Zhou and Zhu 2006). Particularly, in high tech industries, the formation of international alliances is considered to be a necessary strategy. Investigating the competitive capability of local companies in high-tech industries, Lin and Guo (2005) find that the average life span of local small and medium sized companies amounts only to 2.5 years. In order to overcome the outdated technology base that causes the premature exit of many local companies, Lin and Guo (2005) urge the necessity to form alliances with international partners that possess advanced technologies. Interestingly, Chinese studies like to refer to the alliance between Changhong (a Chinese TV manufacturer) and Japanese Panasonic, where the Chinese partner successfully gained access to and imitated its partner's technology and became a close competitor in the following years (Zhou and Zhu 2006). Further, Chinese companies consider allying with Western firms as a viable cost-effective strategy to acquire not only advanced technologies but technological and R&D capabilities of the Western partner firms (Fan Zengqiang 2003) Therefore technology-related learning constitutes a major international alliance formation motive for Chinese companies (Chen and Wang 2002; Wu 2007; Liang 2005, Zhou and Zhu 2006). Further, Chinese studies find that the managerial capabilities and decision making processes of local Chinese companies are not sufficiently developed in order to effectively compete in an international environment (Ti Kan Mu, 2003). Particularly, Luo (1999) finds that many firms in China have inferior organizational and managerial capabilities than their counterparts in advanced industrialized countries. Hence, allying with Western companies, Chinese firms aspire to acquire the advanced managerial know-how from their Western counterpart.

For local Chinese companies access to complementary resources, both tangible and intangible, presents another key alliance formation driver (Liu 2005). Interestingly to note, Chinese studies report that local companies increasingly value intangible resources, such as reputational capital or market experience, more strongly than partner's capital (Wang, Qian and Deng, 2003). Seeking complementary intangible resources has thus become an important motive of international alliance formation for Chinese companies.

5. Discussion on the differences

Our interviews strongly indicate that learning-driven motives, technology and management related constitute the most important drivers for international alliance formation for Chinese companies. Similarly, gaining access to international markets is another key alliance motive. Access to capital was a less important motive for the responding firms. The main motivations that arise from these interviews are described in table 1:

Table 1. Comparison of main alliance motives: Chinese vs. Western findings

Main finding 1: Access to international markets is a very important alliance driver for Chinese companies

On the first sight, Chinese and Western companies appear not to differ significantly; Chinese studies report that the key objective of Chinese companies entering international alliances is to gain access to international markets (Yuan, 2007; Liu 2005; Ge, Zhao and Wang 2003; Ti Kan Mu, 2003). Chinese companies are not fully equipped in terms of technological and managerial know-how in order to effectively compete in international markets (Peng 2000), and hence aim to avoid direct competition at all cost. Therefore, by allying with Western companies, Chinese firms aspire to acquire necessary capabilities and knowledge without the need to directly face Western competitors.

Main finding 2: Access to partner's technology and technological capabilities is an important alliance formation driver for Chinese companies

One of the main deficiencies of local Chinese companies is a lack in advanced technologies and technological capabilities (Hitt et al 2004). This significant technology gap is dividing China from the developed market economies (Svetlicic and Rojec, 1994) and consequently hinders local Chinese firms to effectively compete in product technologies with firms from developed market countries. Particularly, Chinese companies cannot develop or offer new and sophisticated products in sufficient quantity and quality to be competitive with firms from other countries (Hitt et al 2004). As a result, Chinese firms seek access to new technology in order to develop products that can be competitive (Gillespie & Teegen, 1995). As the access to advanced technologies is often only attainable by means of foreign alliances (Oliver 1997) the Chinese government soon realized the merits of international alliances as a vehicle to overcome deficiencies in innovation and product development (Shenkar 1990). Hence, with preferential treatment policy, lower income taxes and favourable financing terms, the Chinese government has ever so encouraged its local firms to ally with foreign alliance partner possessing advanced technologies to improve their technological capabilities and to eventually increase Chinese firm's competitiveness in global markets (Keister 1998, Luo 2000; Shenkar and Li 1999). As a result, one of the main concerns of local Chinese companies is to gain access to current technology (Chen and Wang 2002, Liang 2005, Yu, Fang and Han 2004, Wang, Qian and Deng 2003, Zhou and Zhu 2006, Fan 2003). Consequently, Chinese companies are likely to stress the access to advanced technologies as a main alliance motive. In contrast, Western alliance firms usually have relatively sophisticated technologies that provide firm-specific technological advantages and there rarely emphasise the technological capabilities of local partners to be key driver for alliance formation.

Main finding 3: Access to partner's managerial capabilities is an important alliance formation driver for Chinese companies

In our interviews we found that access to advanced management skills is a very important motive to engage in strategic alliances with Western partners. As many Chinese firms are formerly state owned enterprises that have been recently privatised, managers generally have little experience with managing market-oriented, decentralised businesses (McDonald, 1993; Lau, 1998). As a result, management capabilities and decision-making processes are often not well developed in local Chinese firms (Shama 1993; Lyles & Baird, 1994). Consequently, as Chinese firms have had little exposure to modern management concepts, techniques, and processes (Hitt et al 2000), the need to compete in market-oriented economies with more managerially sophisticated competitors forces Chinese firms to seek Western partners with strong managerial capabilities. While Western alliance partners would surely prefer a Chinese partner who has effective managerial capabilities, Western companies generally have the capability compensate for the local partner's deficiency in this area (Hitt et al 2004).

Main finding 4: Access to partner's intangible assets is more important than tangible resources for Chinese companies

Chinese literature reports that local companies increasingly consider intangible assets to be more significant than tangible assets of partner firms (Wang, Qian and Deng, 2003). Initial emphasis on tangible assets such as partner's capital can be explained by the poorly developed financial and capital market of China, where capital had been only attainable at a high cost (Svetlicic & Rojec, 1994; Hitt et al 2000). Hence, by allying with Western companies, Chinese companies could circumvent the capital market problem in the country. As long as financial and capital are markets are not fully developed and the economy remains unstable, attaining partner's capital is likely to remain an important objective of Chinese alliance companies. However, a more recent driving force for Chinese companies to pursue alliances with Western partners is to develop reputational capital. As an increasing share of Chinese consumers grows an affinity for name brands, thereby declining inferior and counterfeit products, Chinese firms prefer to ally with foreign firms having well-known products (Luo 2000). As Hitt et al (2004) observe**,** **"**legitimacy afforded by a firm with a strong global reputation enhances the Chinese partner's ability to compete in global markets, thereby allowing it to earn needed hard currency and achieve growth" (p.176). Consequently, Chinese companies are more likely to select Western partners with strong positive reputations to reduce the perceived risk in the market. In contrast, Western alliance firms are not as dependent on partner's reputational capital as the Chinese partner is. While Western alliance partner would surely appreciate a partner with strong and positive intangible resources, they have lesser need for legitimacy in general, as they bring their (Western) brand names and reputations to the alliance. Therefore Western companies are less likely to emphasize the intangible assets as their Chinese counterparts do. Intangible resources such as reputation and legitimacy are more critical to the Chinese partner as they enhance their access to other resources such as customers, financial resources, and future alliance partners.

6. Conclusions and implication

With a few notable exceptions (Dong and Glaister 2006; Hitt, Ahlstrom, Dacin, Levitas and Svobodina, 2004; Luo, 1997), extant Western literature on Sino-Western alliances has, so far, failed to acknowledge the importance of investigating the strategic motives of Chinese alliance companies and has subsequently treated them as passive partners. In this paper we therefore tried to fill this void by investigating the key drivers of international alliance formation from the perspective of Chinese companies. Our results indicate that initial deficiencies in the Chinese institutional environment have shaped the strategic motives of local companies: accesses to international markets, technological and managerial competences are the most important motives for Chinese companies to enter alliances with Western companies. We have further shown how alliance motives differ among Western and Chinese companies. Apart from some protected sectors where joint venture is a requirement, Western companies are free to choose their entry mode in the Chinese market. While local alliance partners may provide local knowledge and distribution systems, Western partners are not completely dependent on their Chinese partner. Once a basic level of local knowledge is gained and necessary local ties are established, Western partners can venture on by themselves. However, in the case of Chinese companies, allying with Western companies presents a far more urgent strategy.

For example if Western firms realize that access to technology and knowledge is one of the main reasons for their Chinese counterparts to partner with them they can design a knowledge diffusion strategy that enables knowledge transfer of those knowledge assets that can be shared and that prevents unwanted knowledge spill-overs to their Chinese partners. The reluctance of Western companies to share technology and knowledge with their Chinese counterparts is very clearly reported in the Chinese literature (Dong 2004, Zhou and Zhu 2006). This finding is confirmed in our interviews. Understanding these differences is a necessity for both Western and Chinese partners. Acknowledging these differences allows both partner firms to overcome initial differences in expectations, as they re-adjust their alliance strategies to fit their own and their partners' alliance motives.

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